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RUEHGP/AMEMBASSY SINGAPORE 5729
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RUEHCG/AMCONSUL CHENNAI 8484
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UNCLAS SECTION 01 OF 02 COLOMBO 000471

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SUBJECT: SRI LANKA: MIHIN LANKA LOSES MONEY, SUSPENDS OPERATIONS,
BUT PLANS TO CONTINUE

REF: A) 07 COLOMBO 394 B) COLOMBO 346

1. (SBU) Summary: Mihin Lanka, a budget airline started by the government of Sri Lanka a year ago, has been hemorrhaging public money. The airline stopped flying on May 1 when the last of its two wet-leased aircraft was reclaimed after Mihin was unable to make lease payments, but plans to resume operations in June. The company, named for President Mahinda Rajapaksa, and run by officials close to him and his family, has been unsuccessful from the start. The government and several state banks have so far sunk an estimated 3.5 billion Rupees (USD 32 million) into the venture. While Mihin is losing money, it appears clear that officials involved with it are being well paid despite their incompetence. Advocacy groups, seeking accountability for the operation, are hoping to file lawsuits against the Mihin Board and state banks which funded the airline. Rumors persist that the government will merge Mihin with the larger Sri Lankan Airlines, which recently reverted to government management after its split with Emirates Airlines. End Summary.

LOSING MONEY FAST -- AS EXPECTED

2. (SBU) Mihin Lanka, a budget airline started by the government of Sri Lanka in April 2007, had to temporarily stop flying May 1 when the accompany was unable to pay the costs of its remaining wet-leased plane. The company's operations from the start have been marked by amateurish business decisions, mounting debts, and negative income. Despite this, the airline says it intends to resume operations on June 1, again using two aging leased planes.

3. (SBU) In ref A, post predicted that the venture would not go well, as the government of Sri Lanka has a poor track record in running any state-owned operations profitably, including Sri Lankan Airlines prior to its partial privatization a decade ago. We noted that the venture was to be run by friends and family of President Mahinda Rajapaksa (for whom the airline is named -- Mihin is short for Mihindu, which is the Pali name for Mahinda) and that a long list of questionable actions in forming the airline suggested that these people would probably gain personally from its operations, however unprofitable. This all appears to have transpired.

14. (SBU) Local press reports have described numerous poor business decisions made by Mihin management. To begin with, the airline began operations by wet-leasing two planes -- a costly arrangement in which the company paid not only for the planes but all crew and maintenance. Further, the planes it leased were configured with business class seating, despite the intended role of the airline as a budget carrier that would cheaply transport migrant workers. More recently, after months of operation, Mihin bought two new tarmac buses and leased ground handling equipment including moveable boarding stairways -- even though most flights out of Colombo are boarded directly from the jetways of the renovated terminal. Finally, though perhaps not the fault of management, the airline has periodically had to cancel scheduled flights in order to carry President Rajapaksa and his entourage on international trips.

15. (SBU) It has been difficult to obtain a clear picture of how badly the airline is doing financially. It appears to have burned through approximately Rs 3.5 billion (USD 32 million), which equals 0.7% of 2007 government tax revenue of Rs 508 billion. This figure comes from calculations the opposition United National Party (UNP) reported to Parliament on May 6. The UNP alleged that the airline has borrowed extensively from two state-owned financial institutions, the Bank of Ceylon and Lankaputra Bank. The UNP also reported that the airline owes millions of dollars to the state-owned Ceylon Petroleum Corporation in unpaid fuel bills. The government did not refute these charges. The government has reported in budget documents direct Treasury funding to Mihin Lanka of Rs 750 million from 2007 to 2008.

COLOMBO 00000471 002 OF 002

FAMILY MEMBERS AND FRIENDS RUN AND LEND TO MIHIN

16. (SBU) A major reason for Mihin Lanka's dismal performance is that the company is run by Rajapaksa family members and friends with no experience in the aviation industry. The airline was conceived by Sajin Vaas Gunawardena, a Presidential aide and family friend with a track record of involvement in shady procurement deals. He is the company's CEO but has no aviation experience; he is paid Rs 450,000 (\$4,200) monthly -- quadruple the typical salary for a public enterprise CEO. The board of directors includes the President's brother, Defense Secretary Gothabaya Rajapaksa; the President's trusted secretary, Lalith Weeratunga; and Air Force Commander Roshan Goonetilleke. Treasury Secretary P.B. Jayasundera, also close to the president's family and involved in various Rajapaksa-driven state ventures, was initially on the board but has since been placed as chairman of the Sri Lankan Airlines board.

17. (SBU) As a state-owned enterprise, Mihin Lanka is overseen by the Minister of Ports and Aviation, the President's elder brother, Chamal. About half of the company's financing has come from two state-owned banks headed by family friends. Bank of Ceylon Chairman Gamini Wickramasinghe is a marriage relative. Lankaputra Bank until last month was chaired by the father of Mihin CEO Sajin Vaas Gunawardena. The senior Gunawardena resigned amidst criticism for the bank's loans to the airline. Critics noted the Rajapaksa administration had created and funded Lankaputra Bank to provide low interest financing to small and medium private enterprises.

MEDIA AND WATCHDOGS OUTRAGED, BUT AIRLINE PROCEEDS

18. (SBU) According to the Sunday Leader newspaper of May 11, public advocacy groups plan legal action against both Mihin Lanka and Bank of Ceylon. The groups assert that both the airline and the bank are violating the Companies Law of 2007, which holds corporate boards to relatively high standards of business accountability. The cite, as an example, the Mihin board's irresponsibility in giving a high salary to a CEO with no aviation experience.

19. (SBU) Rohana Perera, Commercial Chief of Mihin Lanka, told Econ FSN that the airline intends to resume operations in June. He confirmed reports that the airline is in the process of dry leasing two 19-year old Airbus A320s (without insurance, crew, ground staff,

supporting equipment, maintenance). In order to convert Mihin operations from wet lease to dry lease, the airline has started recruiting flying crew and maintenance staff.

¶10. (SBU) Comment: Having named Mihin Lanka for the president, its management has too much face invested in it to allow it to fail. The government has generally been silent in the face of all the charges of mismanagement and crony capitalism. Rather than refuting these, it continues to highlight to the public the benefits of the airline providing cheap travel for low income Sri Lankans going to work abroad. The government may also see an expedient way forward, as rumors persist that it will merge Mihin with Sri Lankan Airlines, which the government resumed managing in April (ref B). There are even reports the government will add to its investment of face, by giving the Mihin name to the combined venture.

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